



Standard Life Assurance Limited
Heritage With Profits Fund
Principles and Practices of Financial Management

1 January 2009 – 31 December 2009

Report to UK With Profits Policyholders

and

Statement to UK With Profits Policyholders by the
With Profits Actuary

March 2010

Heritage With Profits Fund
Principles and Practices of Financial Management (PPFM)

1 January 2009 – 31 December 2009

Report to UK With Profits Policyholders

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1. Management of UK With Profits Business in the Heritage With Profits Fund and the Exercise of Discretion

We describe how we manage our UK with profits business in our published Principles and Practices of Financial Management. This report relates to our UK with profits business in the Heritage With Profits Fund and refers to the Principles and Practices of Financial Management for the Heritage With Profits Fund (“Heritage PPFM”).

The Board of Standard Life Assurance Limited (“the Board”) has reviewed the operation of our UK with profits business in the Heritage With Profits Fund. It is the Board’s opinion that throughout 2009 this UK with profits business has been managed in accordance with the Heritage PPFM. It is also the Board’s opinion that the exercise of discretion over the period was appropriate, took full account of policyholders’ reasonable expectations, and maintained fairness between different categories of policy and policyholder, and between policyholders and shareholders.

The Board’s opinion takes account of advice from our With Profits Actuary and With Profits Committee on all key aspects of the operation of our with profits business during the period.

The With Profits Committee have confirmed that, during the period

- This UK with profits business has been managed in accordance with the Heritage PPFM and,
- Discretion was exercised in an appropriate manner.

In reaching this conclusion they have relied on the information that we have provided to them.

The With Profits Actuary has made a statement to policyholders that is annexed to this report.

Our review of the operation of our with profits business over the period covered by this report has the following main areas of interest:

- With profits payout values
- Management of with profits assets
- Shareholder transfers

The following sections give more detail. You can find further information about how we manage our with profits business in our ‘Understanding With Profits’ booklets. These are available on our website www.standardlife.co.uk/withprofits.

2. With Profits Payout Values

Most types of with profits policy contain guarantees, usually in the form of a minimum guaranteed amount to be paid on maturity, retirement or death. Regular bonuses may be added over time, increasing the minimum guaranteed amount. In addition, a final bonus may be paid. Guarantees do not normally apply on surrender or transfer.

For the types of with profits policy where regular bonuses may be added we declared new regular bonus rates on 1 February 2009.

For some types of with profits policy where a final bonus may be paid we changed final bonus rates and other payout calculation factors:

- on 27 January 2009 (for all types of payouts)
- on 17 March 2009 (for surrenders and transfers only)
- on 11 August 2009 (for all types of payouts)
- on 13 October 2009 (for surrenders and transfers only).

The final bonus rates and other payout calculation factors set for each type of policy took account of investment performance data relevant to the asset mix for that type and reflected whatever deductions and smoothing applied.

For other types of with profits policy, whether or not a final bonus may be paid, the payout value was calculated directly for each policy using the applicable investment performance data relevant to the asset mix for its type and reflected whatever deductions and smoothing applied. We paid any applicable guaranteed minimum amount if this was higher.

For the With Profits Pension Annuity the declared rates of return were based on investment performance data relevant to the asset mix for that business and whatever deductions and smoothing applied.

When we review with profits payout levels we decide the extent of any smoothing of investment returns it is appropriate to provide in payout values. Smoothing gains and losses fall primarily to remaining with profits policyholders. We take account of the need to protect their interest when we decide how much smoothing to provide. As a result of the severe market falls during 2008 we had taken action with the aim of reducing smoothing losses in the fourth quarter of that year. We restored the normal extent of smoothing for all types of payouts in the fourth quarter of 2009.

We state above that although most types of with profits policies contain guarantees there are some circumstances where no guarantees apply to the amount payable, for example on most surrender and transfer claims. In particular, we may reduce the unit price for unitised policies, in accordance with the individual terms and conditions of the policy, where the fair payout is lower than the value based on the unit price without a reduction. However for certain types of payouts during the period we did not reduce unit prices even though we could have done so under the terms of the policy. This was the case, for example, when:

- the proceeds of a pension policy were used to secure directly an annuity or tax-free cash and an annuity;
- the payout was made from a pension policy on or after the retirement date chosen at the start of the policy.

This discretionary practice could change in future but only if it was necessary in order to maintain fairness between with profits investors.

Our current practice for most with profits policies is to use asset shares (together with certain discretionary adjustments including any smoothing) to set fair payouts for with profits policyholders. When calculating asset shares, we make deductions for the assessed costs of guarantees. These deductions vary between types of policy, reflecting the nature of the guarantees provided. The assessed costs of guarantees fluctuate, for example they tend to increase if the assets backing with profits policies fall in value, and we therefore adjust the deductions from time to time. We increased the deductions in early 2009 but then reduced them in early 2010 following a review in December 2009.

During 2009 we continued to make distributions of the Inherited Estate by enhancing with profits payouts.

Errors occur from time to time in the operation of with profits and other types of business. Where such errors are discovered, steps are taken to ensure that they are corrected and, where appropriate, additional controls are put in place to reduce the risk of future errors. If appropriate, additional payments are made to policyholders whose payouts have been adversely affected by such errors.

There were no errors that we are aware of that compromised our compliance with the Heritage PPFM.

3. Management of With Profits Assets

The investment strategy for our with profits business aims to achieve competitive returns, whilst still maintaining an appropriate level of financial strength and meeting all contractual obligations to policyholders. We decide what asset mix to hold by considering the extent of guarantees for each class of with profits policy, and the appropriate balance between risk and expected return. During 2009 we regularly reviewed the asset mix for each class of with profits business.

When we invest in assets with more variable values, there is a higher risk that the assets will have low values when we need to make payouts to policyholders. In particular the asset share of a with profits policy could be worth less than the guaranteed benefits. In this case the shortfall has to be met. The higher the level of guarantees for a class of policy, then the higher the proportion of assets backing that class of policy which we may have to invest in lower-risk assets with more stable values.

The table below shows the approximate proportion of equity and property in the asset mix for different types of with profits business at 31 December 2009. The table also shows the estimated return achieved on the asset mix during 2009:

	Equity + property 31.12.2009	Estimated Return*
- Stakeholder With Profits Fund	60.1%	19.1%
- Pooled With Profits Fund		
- Unitised Pensions with minimum unit price growth rate of 4% a year	18.8%	3.6%
- Unitised Life policies with minimum unit price growth rate of 3% a year		
- With Profits Bond	64.5%	8.6%
- With Profits Pension Annuities	52.1%	7.3%
- Unitised Pensions with minimum unit price growth rate of 0% a year	57.1%	7.9%
- Unitised Life policies with minimum unit price growth rate of 0% a year (other than With Profits Bonds)		
- Most other with profits investments	44.8%	6.2%

* This is the rounded down estimated investment return before tax for the period from 1 January 2009 to 31 December 2009.

4. Shareholder Transfers

Shareholders are entitled to certain payments from the Heritage With Profits Fund (the Fund) in accordance with the terms of the Scheme of Demutualisation, as described in the Heritage PPFM. The Heritage PPFM also explains that the shareholder entitlement to these payments is subject to the Fund being able to continue to meet its liabilities. A shareholder transfer in this respect for the year ended 31 December 2008 was made from the Fund in March 2009.

In 2009 we effected a transaction which removed a risk to the tax treatment of future shareholder transfers from the Fund by converting some of these future transfers into the form of loan repayments. Although this reduction in risk to shareholder value has no direct benefit to the Fund it helps to support the financial strength of Standard Life and therefore the security of policyholders' benefits. We set the terms and conditions for the transaction so that the position of the Fund would be unaffected. A small payment is, however, being made to the Fund in respect of the transaction and in addition we have made an undertaking that in the event of the Fund being found to have suffered any loss from the transaction it will be made good from shareholder funds.

5. Changes to the Heritage With Profits Fund PPFM

The Heritage PPFM has been maintained in accordance with regulatory requirements throughout 2009. Changes were made to the Heritage PPFM during 2009: the revised Heritage PPFM document incorporating these changes is dated 30 June 2009. No changes were made to principles or practices but various minor amendments were made to improve clarity, consistency and accuracy of wording.

ANNEX

Statement to UK with-profits policyholders by the With-Profits Actuary

The Financial Services Authority has set out regulations that require a firm transacting with-profits business to appoint a With-Profits Actuary, who has a number of statutory responsibilities in relation to that business. As With-Profits Actuary to Standard Life Assurance Limited, I have a statutory duty to advise the firm when it exercises its discretion in the management of its with-profits business.

The regulations require me to inform you, as policyholders, whether I regard the accompanying report as taking, or having taken, your interests into account in a reasonable and proportionate manner. I am required to do this also in relation to the discretion Standard Life Assurance Limited has exercised in its management of with-profits business, for example in its declarations of bonuses on with-profits policies.

I confirm that, in my opinion, and based on the information and explanations provided to me by the firm, and taking into account where relevant the rules and guidance in the FSA Handbook, the annual report and the discretion exercised by the firm during 2009 may be regarded as having taken the interests of the relevant classes of the firm's with-profits policyholders into account in a reasonable and proportionate manner.

Douglas Morrison FFA
With-Profits Actuary
March 2010